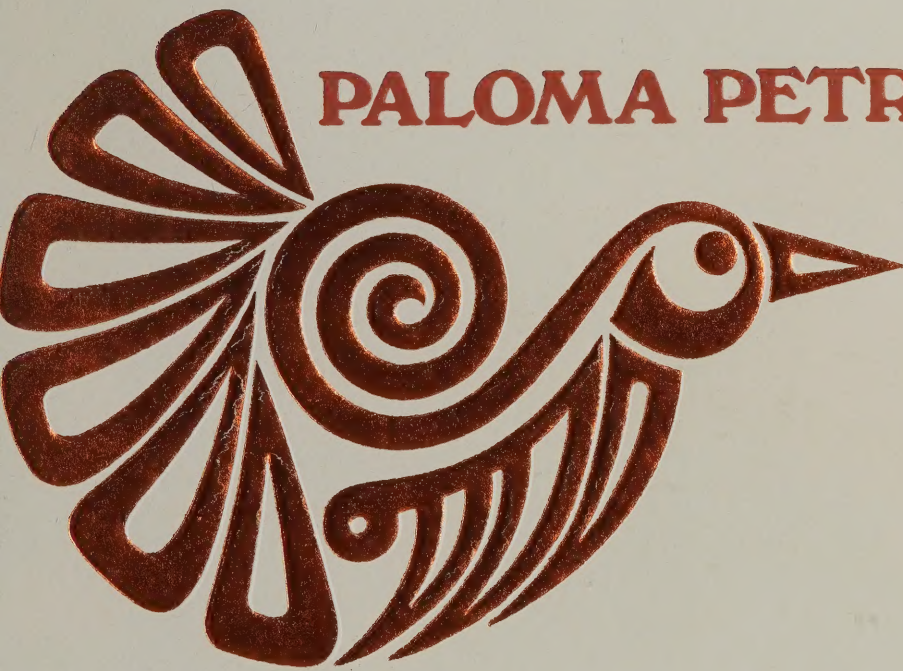




**PALOMA PETROLEUM LTD.**





# Paloma Petroleum Ltd.

## CONSOLIDATED STATEMENT OF EARNINGS

Six Months ended June 30, 1976  
(with comparative figures for 1975)



PALOMA PETROLEUM LTD.

AR14

Interim Report

Six months ended June 30, 1976

|                                                                                                                                              | 1976<br>(Unaudited) | 1975<br>(Unaudited) |
|----------------------------------------------------------------------------------------------------------------------------------------------|---------------------|---------------------|
| Revenue:                                                                                                                                     |                     |                     |
| Oil and gas .....                                                                                                                            | \$1,316,726         | \$897,850           |
| Hotel, real estate and<br>cafeteria gross operating<br>profits .....                                                                         | 378,430<br>21,139   | —<br>3,938          |
| Interest and other income ..                                                                                                                 | 1,716,295           | 901,788             |
| Expenses:                                                                                                                                    |                     |                     |
| Production of oil and gas ..                                                                                                                 | 145,828             | 97,159              |
| Administrative .....                                                                                                                         | 317,706             | 188,863             |
| Interest and finance charges                                                                                                                 | 723,867             | 107,032             |
| Depreciation .....                                                                                                                           | 136,226             | 25,289              |
| Depletion .....                                                                                                                              | 149,568             | 51,605              |
|                                                                                                                                              | 1,473,195           | 469,948             |
| Net earnings before<br>undernoted items .....                                                                                                | 243,100             | 431,840             |
| Income taxes:                                                                                                                                |                     |                     |
| Current .....                                                                                                                                | 114,000             | 109,000             |
| Deferred .....                                                                                                                               | 190,000             | 178,000             |
| Province of Alberta                                                                                                                          | (175,000)           | (142,000)           |
| Royalty Credit .....                                                                                                                         | 129,000             | 145,000             |
| Earnings before interest of<br>minority shareholders and<br>extraordinary item .....                                                         | 114,100             | 286,840             |
| Interest of minority<br>shareholders in net loss of<br>subsidiary companies .....                                                            | 14,657              | —                   |
| Earnings before extraordinary<br>item .....                                                                                                  | 128,757             | 286,840             |
| Extraordinary item:                                                                                                                          |                     |                     |
| Reduction of deferred<br>income taxes resulting<br>from application of drilling<br>and exploration expenses<br>by certain subsidiaries ..... | 31,000              | 70,000              |
| Net earnings .....                                                                                                                           | \$ 159,757          | \$356,840           |
| Net earnings per share:                                                                                                                      |                     |                     |
| Before extraordinary item ..                                                                                                                 | \$ .03              | \$ .07              |
| Extraordinary item .....                                                                                                                     | \$ .01              | \$ .02              |
|                                                                                                                                              | \$ .04              | \$ .09              |



PALOMA PETROLEUM LTD.



**to the Shareholders:**

Paloma Petroleum Ltd. increased its gross revenues 90% during the first half of 1976 as a result of increased gas production at higher wellhead prices and also through the inclusion of the operations of Compass Investments of Alberta Limited. Cash flow from operations increased marginally over the corresponding period for 1975, with higher debt servicing costs offsetting gains made from increased production. Financial highlights for the six months ended June 30, 1976 are as follows:

|                                               | 1976        | 1975      |
|-----------------------------------------------|-------------|-----------|
| Gross income .....                            | \$1,716,295 | \$901,788 |
| Cash flow from operations ...                 | 601,067     | 541,734   |
| Per share .....                               | 14c         | 13c       |
| Net earnings before extraordinary items ..... | 128,757     | 286,840   |
| Per share .....                               | 3c          | 7c        |
| Net earnings .....                            | 159,757     | 356,840   |
| Per share .....                               | 4c          | 9c        |

Gross natural gas production increased 24% to 1,725 mmcf/d compared to 1,396 mmcf/d for the first six months of 1975. Crude oil and condensate production increased 9% to 74,855 bbls. compared to 71,589 bbls. for the same period in 1975.

Paloma's drilling results are tabulated below:

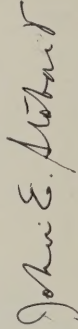
|                     | Gross | Net   |
|---------------------|-------|-------|
| Wells drilled ..... | 28    | 10.62 |
| Gas .....           | 20    | 8.79  |
| Oil .....           | 1     | 0.125 |
| Dry .....           | 7     | 1.70  |

New Alberta gas production went on-stream during the first half of 1976 at Hines Creek, Sedalia and Jarraw. At Hines Creek, where Paloma has an 8.33% interest, gas sales commenced at a rate of 4.8 mmcf/d. The Company has a 25% interest at Sedalia where we sell 5 mmcf/d and a 50% interest at Jarraw where we have been selling 2 mmcf/d and expect to increase sales to 6 mmcf/d, later this year, as a result of six recently drilled gas wells.

At Wainwright, Alberta we commenced gas deliveries on July 9, 1976 from our recently developed gasfield near the Town of Wainwright. Initial rates from six wells ranged between 1.0 and 2.0 mmcf/d. By October, a total of ten wells will be connected and a 600 H.P. compressor will be installed; a producing rate of 4 to 5 mmcf/d is then expected. The Company's interest is 72%. Single gas wells discovered at Ferrybank and Nestow, Alberta in late 1975 are just going on-stream. At Nestow, we have a 50% interest in production of 3 mmcf/d and at Ferrybank, we have an 18.75% interest in production expected to be 1.5 mmcf/d.

We are very pleased with the success of exploration drilling during the period and can report commercial gas discoveries at Sibbald, Lait, Flat Lake, Cardinal Lake and Whitelaw, all in Alberta. We also participated in a successful oil step-out well at Barnwell, Alberta.

In the United States, Paloma has a 33 1/3% interest in 103,300 acres in the Arkoma Basin of Arkansas where we plan to drill an exploratory well in September 1976. In the Oklahoma portion of the Arkoma Basin, we have a 50% interest in 12,162 acres on which we are attempting to have a farmout well drilled. In Webster Parish, Louisiana, where we have a 25% interest in 8,000 acres, a 13,000 ft. exploratory well will be drilled by another company on a farmout later this year.



August 30, 1976.  
Calgary, Alberta.

John E. Stobart,  
President.

|                                                                              | 1976<br>(Unaudited) | 1975<br>(Unaudited) |
|------------------------------------------------------------------------------|---------------------|---------------------|
| Source of funds:                                                             |                     |                     |
| Net earnings before extraordinary item .....                                 | \$ 128,757          | \$286,840           |
| Add (deduct) items not affecting working capital:                            |                     |                     |
| Depreciation .....                                                           | 136,226             | 25,289              |
| Depletion .....                                                              | 149,568             | 51,605              |
| Deferred income taxes .....                                                  | 190,000             | 178,000             |
| Other .....                                                                  | (3,484)             | —                   |
| Working capital provided from operations .....                               | 601,067             | 541,734             |
| Proceeds from sale of fixed assets .....                                     | 302,405             | 10,200              |
| Increase in bank loans .....                                                 | 500,000             | 273,000             |
| Other assets .....                                                           | 18,105              | —                   |
| Total working capital provided .....                                         | 1,421,577           | 824,934             |
| Use of funds:                                                                |                     |                     |
| Purchase of property plant and equipment .....                               | 1,530,706           | 288,020             |
| Reduction of long-term debt, including amounts of reclassified as current .. | 992,526             | 268,731             |
| Financing costs .....                                                        | 20,595              | —                   |
| Total working capital applied .....                                          | 2,543,827           | 556,751             |
| Increase (decrease) in working capital .....                                 | (1,122,250)         | 268,183             |
| Working capital at beginning of period .....                                 | 263,255             | 238,072             |
| Working capital (deficiency) at end of period .....                          | \$ (858,995)        | \$506,255           |





# Highlights of Operations

**FINANCIAL**

|                                                      | 1976         | 1975         |
|------------------------------------------------------|--------------|--------------|
| Gross income . . . . .                               | \$ 6,567,973 | \$ 1,965,366 |
| Cash flow from operations . . . . .                  | 1,501,157    | 1,274,158    |
| Per share . . . . .                                  | .36          | .31          |
| Net earnings before<br>extraordinary items . . . . . | 284,065      | 659,688      |
| Per share . . . . .                                  | .07          | .16          |
| Net Earnings . . . . .                               | 433,565      | 735,288      |
| Per share . . . . .                                  | .10          | .18          |

**OPERATIONS**

|                                                            |            |             |
|------------------------------------------------------------|------------|-------------|
| Natural Gas sales (Mcf) . . . . .                          | 3,719,000  | 2,679,000   |
| Daily average . . . . .                                    | 10,189     | 7,340       |
| Crude oil and condensate<br>production (barrels) . . . . . | 151,745    | 159,816     |
| Daily average . . . . .                                    | 416        | 438         |
| Proven reserves:                                           |            |             |
| Natural gas (Mcf) . . . . .                                | 93,172,000 | 103,238,000 |
| Crude oil and condensate<br>(barrels) . . . . .            | 1,975,347  | 1,932,332   |
| Probable additional reserves:                              |            |             |
| Natural gas (Mcf) . . . . .                                | 8,168,000  | 4,170,000   |
| Crude oil and condensate<br>(barrels) . . . . .            | 51,377     | 482,047     |
| Land holdings including<br>royalty interests:              |            |             |
| Gross acres . . . . .                                      | 4,468,105  | 4,317,615   |
| Net acres . . . . .                                        | 302,120    | 319,785     |

## Annual Meeting

The Annual General Meeting of the Shareholders will be held on May 16, 1977, in Salon E, Holiday Inn, 708 - 8th Avenue S.W., Calgary, Alberta, at 2:00 P.M., Calgary time.



## Report of the Directors to the Shareholders



The Company increased its sales of natural gas by 39% over the previous year as a result of new gas discoveries going on-stream. Thirty-five gas wells and one oil well resulted from participation in the drilling of 54 wells during the year. In addition, there were several gas wells discovered on our land by other companies drilling under farmout agreements. Our 1976 exploration efforts resulted in the discovery of new Alberta gas reserves at Acadia, Belloy, Cardinal Lake, Flat Lake, Lait, Jarrow, Stanmore and West Hotchkiss. In early 1977 we drilled a successful oil well immediately east of the Leduc field in Alberta. A well drilled on our Arkansas acreage in 1976 tested gas in non-commercial quantities. We have concentrated our exploration activity in Alberta where the investment opportunity is most attractive and secondly in British Columbia, where we participated in two unsuccessful wells this past year. Although 36% of our oil production is derived from Saskatchewan, we do not plan any further drilling there until the Government policy permits profits commensurate with investment. We shall tailor our 1977 exploration and development budget to optimize the production levels in those areas where we have gas contracts and also to add to our land inventory whenever there are opportunities to acquire attractive acreage.



Dunvegan and Belloy fields continue to be the major source of revenue representing 69% of our gas production. We experienced reduced gas sales at Dunvegan, for most of the year, due mainly to inadequate pipeline facilities serving the area. This problem should be rectified with the construction of a larger pipeline to be completed in April 1977. Gas deliveries from Belloy were also down during the year because certain wells have been watering out. Recent drilling in the area has been successful and we expect to raise the production level at Belloy during 1977. We installed compression and tie-in facilities at Nestow and Wainwright during the year and will be constructing similar facilities for our newly discovered gas areas in order to place them on-stream as soon as possible. We are fortunate, in light of mid-1976 indications of a gas surplus in Alberta, to have 95% of our gas reserves under contract. We will be deferring some projects which will be affected by market delays resulting from the gas surplus.

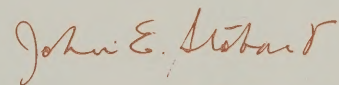
The Company currently receives an average wellhead price of \$1.24 per thousand cubic feet of natural gas and \$9.75 per barrel of oil with price increases anticipated in 1977.

Paloma's revenue from the sale of gas and oil increased 55% from \$1,965,366 in 1975 to \$3,048,384 in 1976. Revenue from hotel, restaurant and real estate operations amounted to \$3,422,570 and compare favorably with revenues prior to our December 1975 acquisition of Compass Investments of Alberta Limited. In spite of increased revenues our net earnings have decreased from \$735,288 in 1975 to \$463,022 in the current year. This is a result of a substantial increase in debt carrying costs as well as the increase in all other expenses. We realized \$1,049,464 on the sale of our equity in another oil company, in early 1977, in order to provide additional cash to the company.

We are pleased that Mr. G. Clarence Elliott, of Winnipeg, joined our board during the year. Mr. Elliott spent 35 years in the Investment Division of Great West Life Assurance Company and was the Vice-President, Investment Policy at the time of his retirement in July 1975.

We are grateful for the competence of our relatively small staff who have made it possible to manage a high level of activity during the past year and we look forward to another year of achievement in 1977.

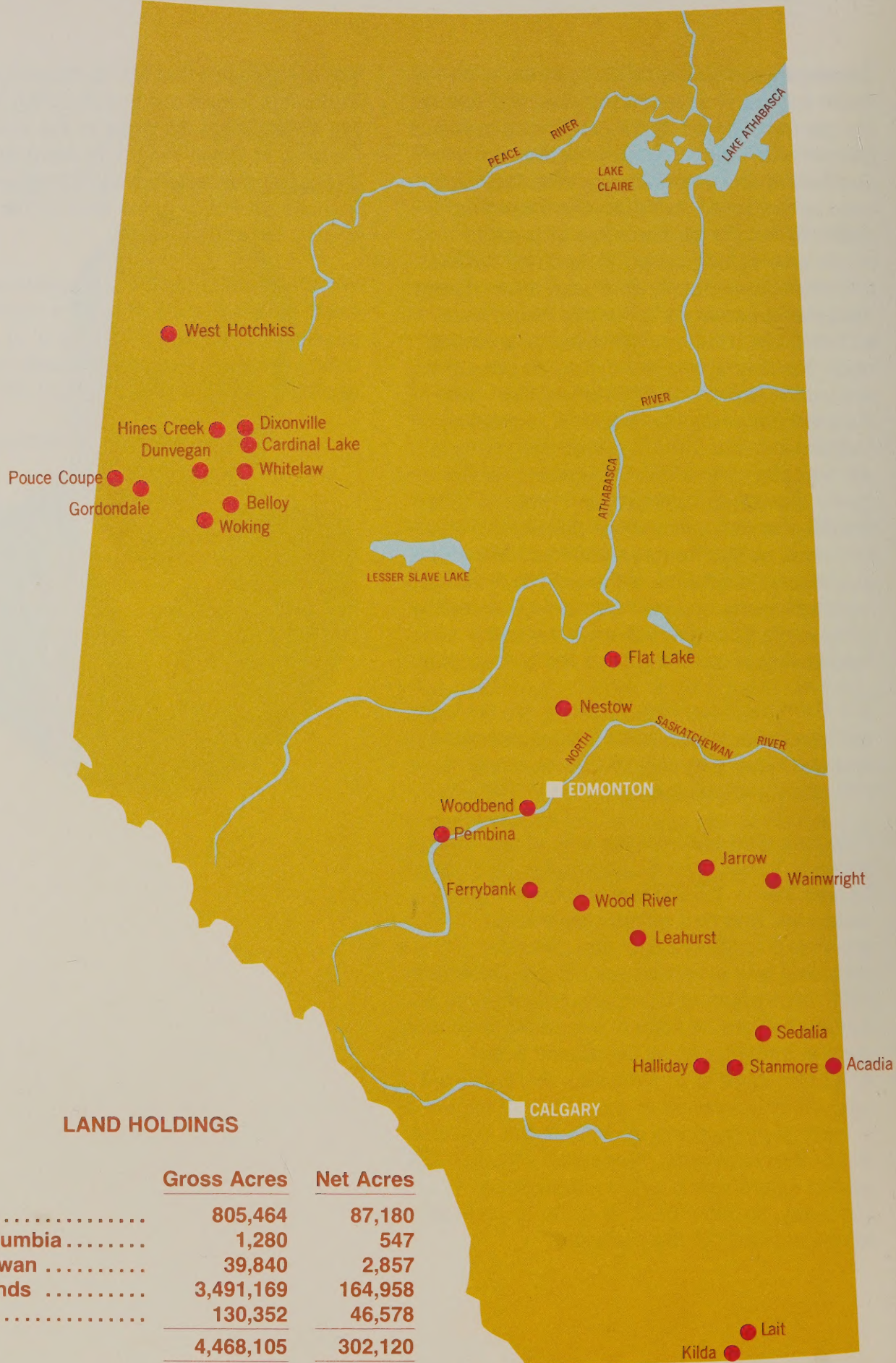
On behalf of the Board of Directors,



President

March 31, 1977  
Calgary, Alberta







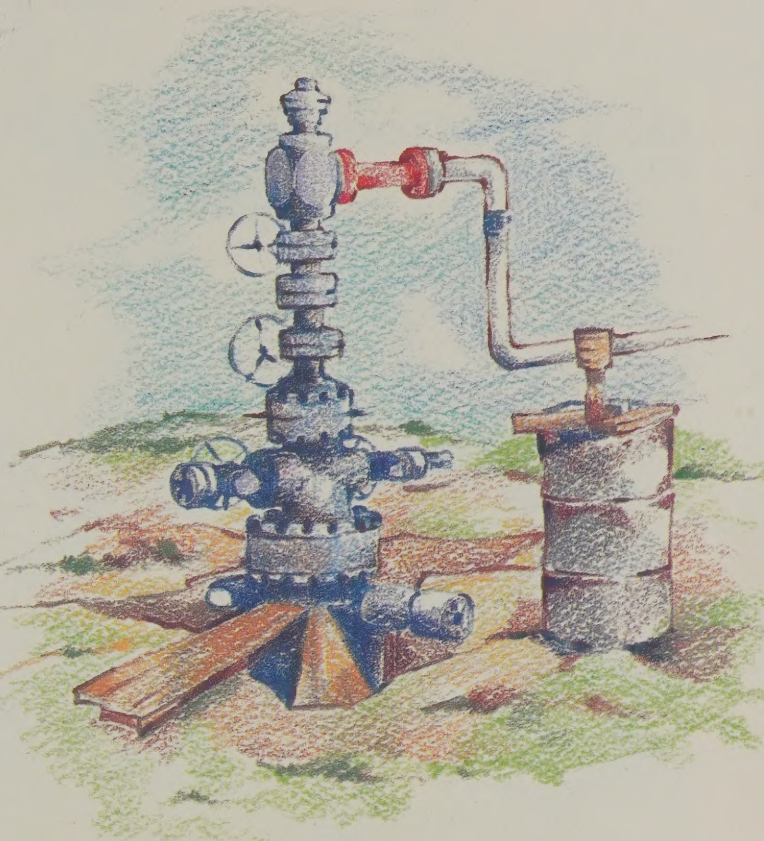


# Review of 1976 Operations

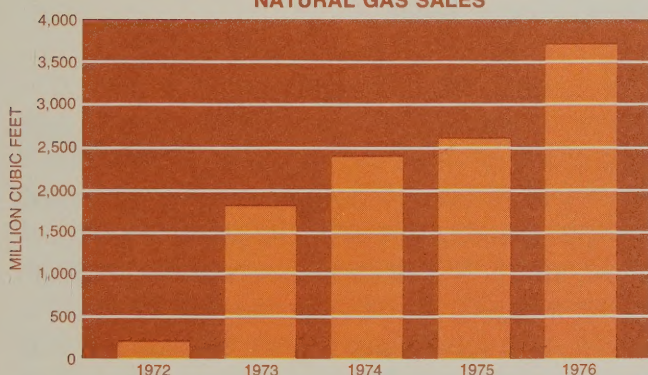
## SUMMARY OF DRILLING ACTIVITY

Paloma Petroleum Ltd. and two of its subsidiaries, Compass Resources Ltd. and Conquest Oil & Mining Ltd. were all active in drilling during 1976. They participated in the drilling of 41 exploratory wells and 13 development wells. All of the development wells and 23 of the exploratory wells were successful. All of the wells, excepting one Wainwright oil well, were gas discoveries. Paloma's interest in wells drilled is as follows:

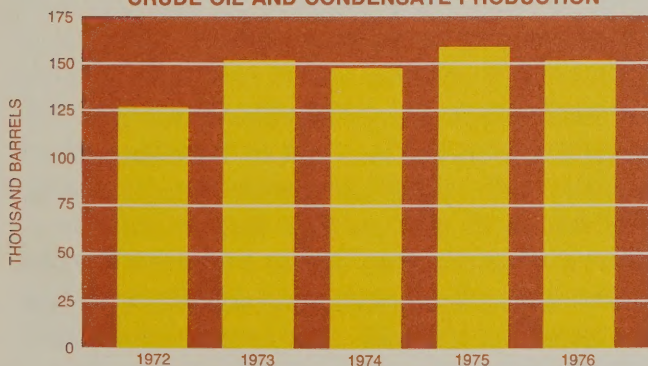
|                       | Gross | Net  |
|-----------------------|-------|------|
| Exploratory . . . . . | 41    | 13.6 |
| Productive . . . . .  | 23    | 8.4  |
| Dry . . . . .         | 18    | 5.2  |
| Development . . . . . | 13    | 6.4  |



**PRODUCTION (Before Royalties)**  
**NATURAL GAS SALES**



**CRUDE OIL AND CONDENSATE PRODUCTION**



## Production

### NATURAL GAS

Sales of natural gas increased 39% over the prior year's level as the result of new production at Jarrow and Sedalia. A further increase is anticipated for 1977 as new Alberta gas is placed on-stream at Acadia, Dixonville, Flat Lake and Stanmore as well as increased production from the Belloy, Dunvegan and Jarrow fields.

### OIL AND CONDENSATE

Production of crude oil and condensate was down 5% from the previous year. This drop to 151,745 barrels, in 1976, from 159,816 barrels, in 1975, represents a natural production decline in our oil wells.



# Reserves (Before deducting royalties)

December 31, 1976

|                                         | <u>Proved</u>     | <u>Probable<br/>Additional</u> | <u>Total</u>       |
|-----------------------------------------|-------------------|--------------------------------|--------------------|
| <b>CRUDE OIL AND CONDENSATE (BBLs.)</b> |                   |                                |                    |
| Province of Alberta                     |                   |                                |                    |
| Pembina Area . . . . .                  | 660,910           | —                              | 660,910            |
| Rainbow Area . . . . .                  | 147,119           | —                              | 147,119            |
| Other . . . . .                         | 682,199           | 51,377                         | 733,576            |
| Subtotal . . . . .                      | <u>1,490,228</u>  | <u>51,377</u>                  | <u>1,541,605</u>   |
| Province of Saskatchewan                |                   |                                |                    |
| Parkman Area . . . . .                  | 163,545           | —                              | 163,545            |
| South Eureka Area . . . . .             | 152,148           | —                              | 152,148            |
| Other . . . . .                         | 169,426           | —                              | 169,426            |
| Subtotal . . . . .                      | <u>485,119</u>    | <u>—</u>                       | <u>485,119</u>     |
| TOTAL . . . . .                         | <u>1,975,347</u>  | <u>51,377</u>                  | <u>2,026,724</u>   |
| <b>NATURAL GAS (MCF)</b>                |                   |                                |                    |
| Province of Alberta                     |                   |                                |                    |
| Peace River Area . . . . .              | 63,618,000        | —                              | 63,618,000         |
| Other . . . . .                         | 29,554,000        | 8,168,000                      | 37,722,000         |
| TOTAL . . . . .                         | <u>93,172,000</u> | <u>8,168,000</u>               | <u>101,340,000</u> |

As at December 31, 1976 total proven and probable natural gas reserves totalled 101,340 million cubic feet, compared to 107,408 million cubic feet at December 31, 1975. This downward revision of gas reserves was due to the performance of the Belloy and Dunvegan fields where certain wells had not measured up to earlier expectations. A corresponding decrease in condensate reserves occurred as all our condensate comes from these two fields. Additional development wells planned for Belloy and Dunvegan in 1977 should restore the reserves to the earlier estimates or higher. Partially offsetting declines at Belloy and Dunvegan were new reserves found, principally at Jarrow, Leahurst, Nestow, Flat Lake and Wainwright, Alberta.

## PRICES AND MARKETS

The Canadian Government policy is to allow the price of domestic oil to rise gradually to world price levels and also to allow gas prices

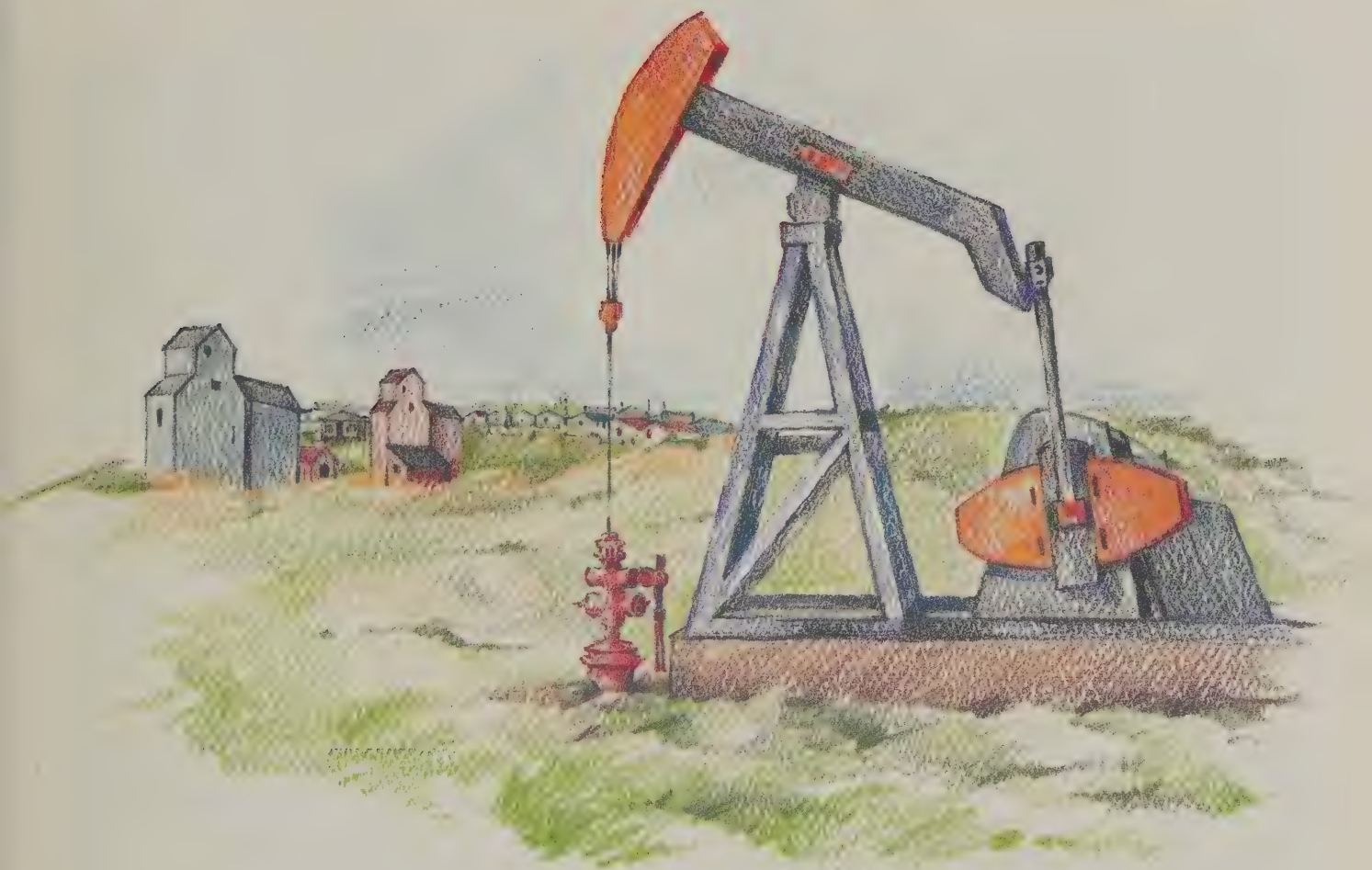
to reach parity with oil prices on a comparative heating value basis.

The current average wellhead price for domestic gas is \$1.24 per thousand cubic feet as a result of price increases of 15.5 cents July 1, 1976 and 10 cents per thousand cubic feet on January 1, 1977. Oil prices rose by \$1.05 and \$.70 per barrel, on corresponding dates, bringing current average wellhead prices up to \$9.75 per barrel. Additional price increases are expected for both gas and oil in order to reduce the disparity between Canadian and increasing world prices.

An excess gas supply situation became evident during the last half of 1976 and the industry faces possible market delays of one to three years for new gas discovered in Alberta. Paloma is fortunate in that 95% of its gas reserves are under contract; however, we are deferring projects which will be affected by market delays.



# Canadian Operations



## DUNVEGAN

Paloma's prime source of revenue comes from the Dunvegan Gas Unit located in the Peace River area of Alberta. Our share of sales from the unit was 2,143 MMcf of gas and 19,525 barrels of condensate for 1976. Production was restricted from May to year end due to inadequate pipeline facilities serving the Dunvegan area as well as a general reduction in gas sales by the industry. With the construction of a larger pipeline, to be completed in April, 1977, and a program of development drilling planned for 1977, unit production should be at a daily level of 180 MMcf by the end of 1977 as compared with a daily average of 137 MMcf for this past year. This will increase Paloma's daily production to 8.1 MMcf from the 1976 average of 5.9 MMcf.

## BELLOY

Paloma has a 21.875% working interest in most of the Belloy field which produced gas at an average daily rate of 7.5 MMcf during this past year. A development drilling program commenced at the end of 1976, with results to date, indicating significant increases in field production rates.



## JARROW

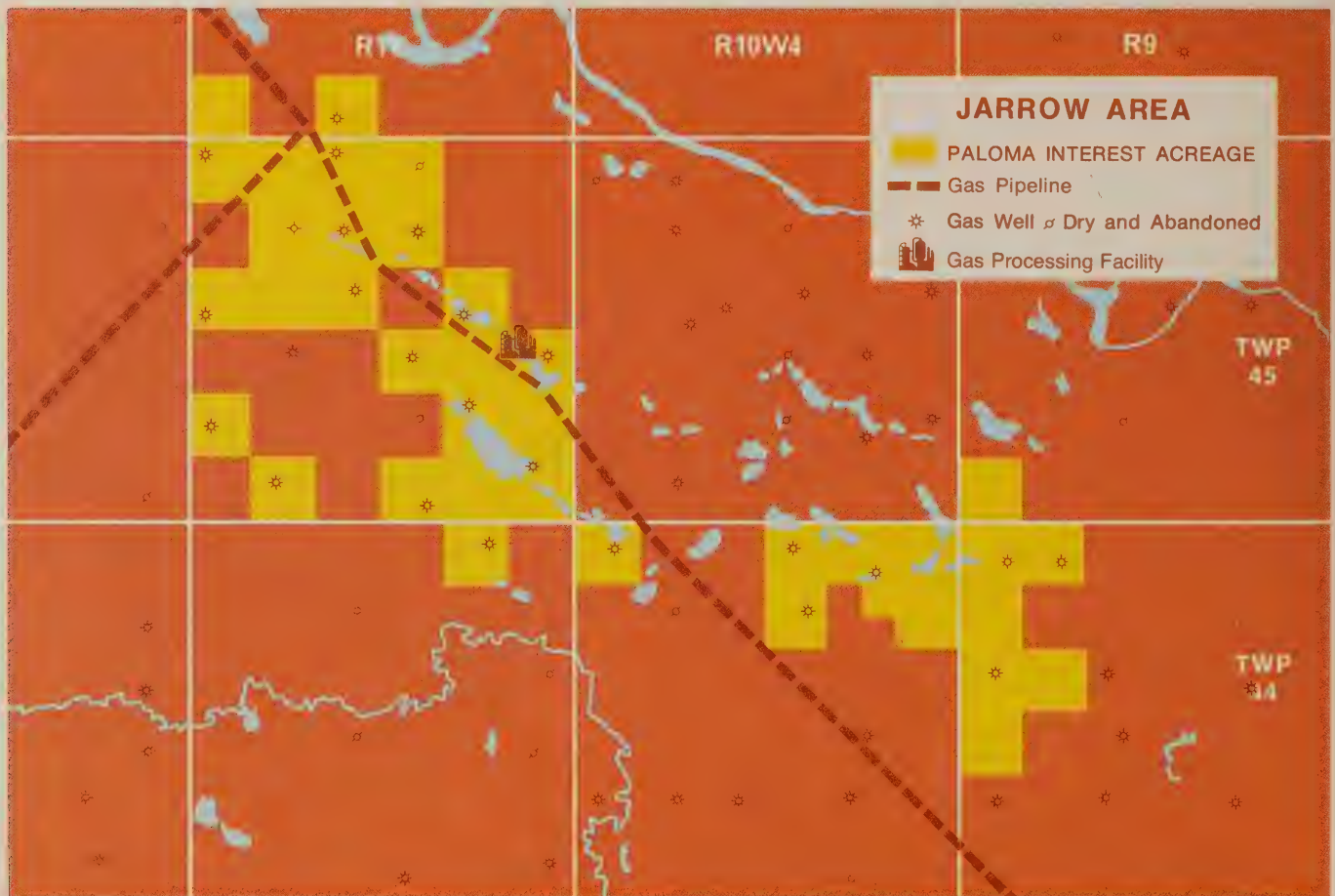
The Company, along with its partners, drilled eight wells in this area of East Central Alberta resulting in seven completed gas wells. In addition all of eleven wells drilled by a third party, on our acreage, under a farmout agreement were completed as potential gas wells. Additional gathering lines were installed during the year and our compressor capacity is now being increased. We anticipate our 1977 net daily gas sales to average 2.5 MMcf under our sales contract with Trans Canada Pipe Lines Limited. As a result of the extensive 1976 drilling program, much of the 22,926 acres (7,278 net acres) has been developed but we anticipate additional drilling to realize the full potential of this area.

## PEACE RIVER AREA

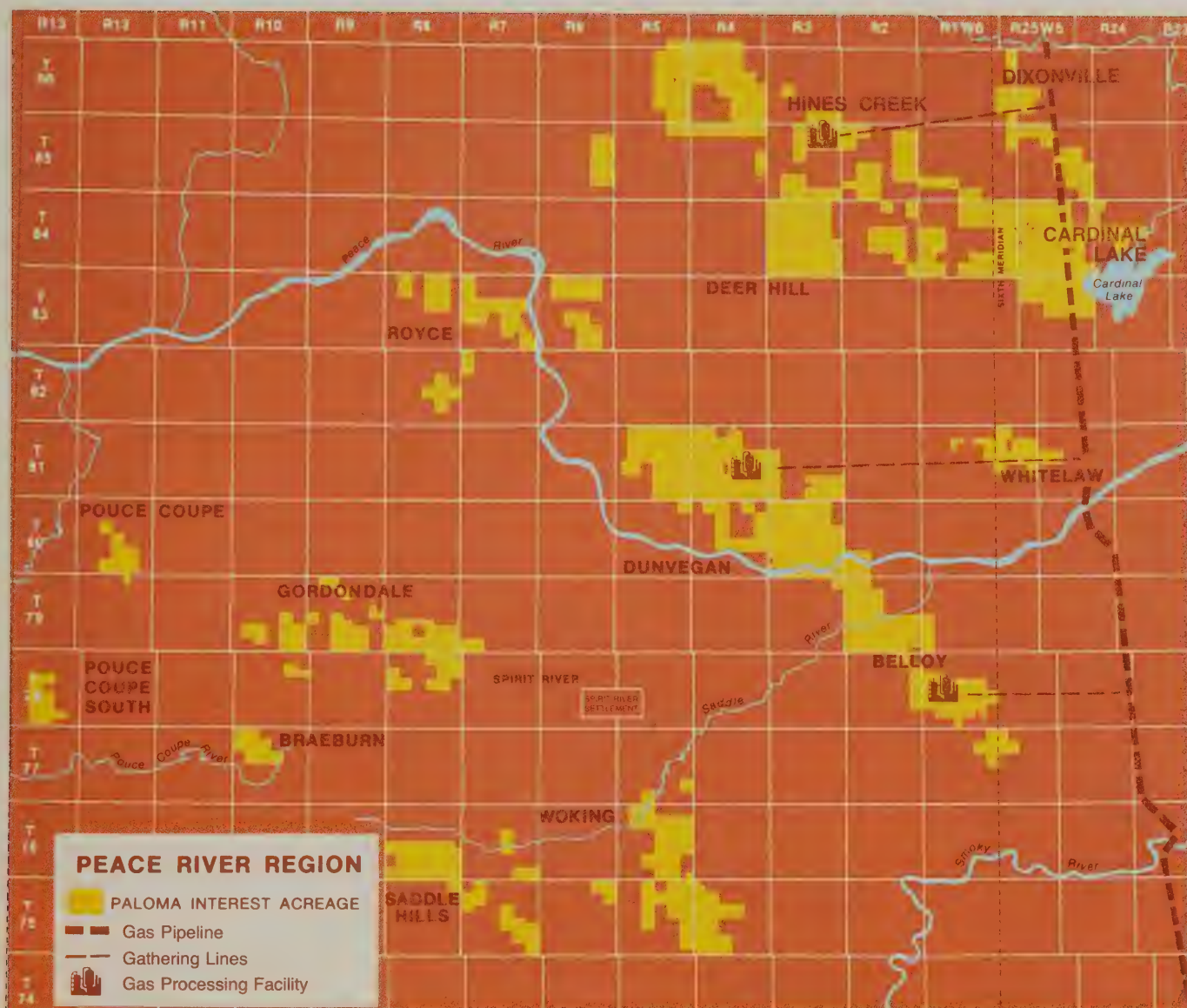
This is a highly prospective gas area noted for a great number of producing zones. The Company has interests in 417,666 gross acres with over 80% of our 25,422 net acres still undeveloped. We believe that there is considerable exploration potential in this area. Developments of particular interest are as follows:

### Hines Creek

Two gas wells were put on-stream May 1, 1976, selling gas to Alberta & Southern Gas Co. Ltd. at a daily contract rate of 4.8 MMcf. We are forecasting steady production at this rate throughout 1977. Our interest in the field is 8.33% and the Company is represented in 72,160 gross acres (3,592 net acres).







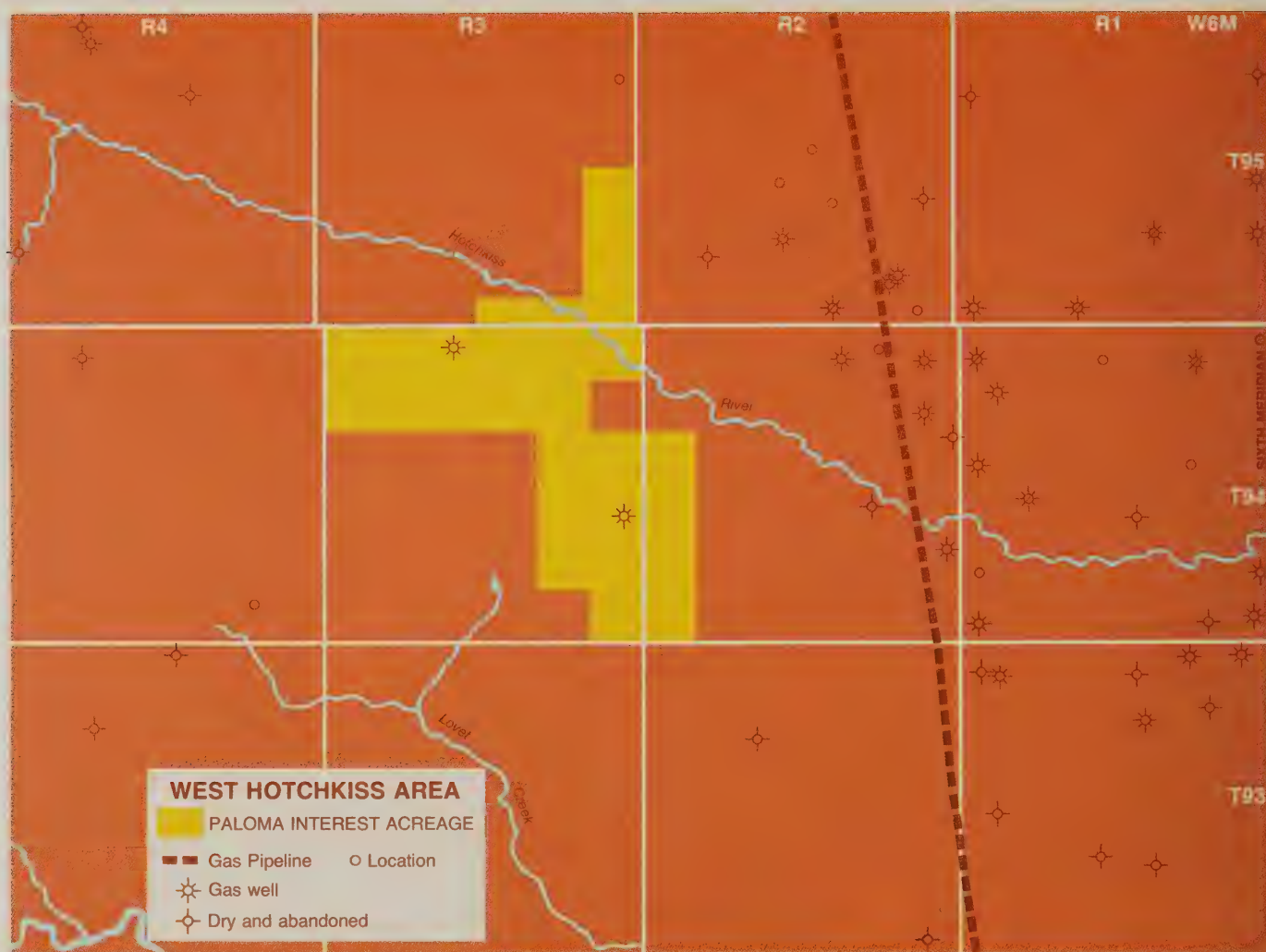
### Dixonville

A third gas well was discovered on this acreage in 1977 and all three wells are scheduled to go on-stream in the last half of 1977, producing at the daily rate of 4 MMcf. The Company has a 8.33% interest in the 14,080 acres comprising this play.

### Cardinal Lake

Paloma participated in two gas discovery wells drilled during 1976 and we expect to be selling gas in this area by the end of 1977. The Company holds a 4.77% interest in the 39,226 acre block and further drilling is planned for 1977.





## West Hotchkiss

The Company participated in two successful gas wells drilled in late 1976 with interests varying between 11.5% and 16.5% in 16,000 acres which were acquired through farmout drilling and purchase from the Crown. Our lands are located five miles west of a major trunk gas pipeline and we are currently discussing a gas contract with a potential buyer. The area has exciting gas potential and we are planning additional wells to be drilled in 1977.

## OTHER AREAS

The Company conducted additional exploratory and development activities in East Central and Southern Alberta. The main areas of interest are as follows:

### Wainwright

The Company has 8,142 acres in Wainwright (3,886 net acres) where we now have 11 gas wells and two oil wells on production. We installed gathering lines and a compressor during the year and are currently selling 1.3 MMcf per day to Northwestern Utilities Ltd. of which the Company's share is 65%. We expect to increase the rate of production



through further development drilling in 1977. Two oil wells currently producing an aggregate of 30 barrels per day, on primary production, are situated in an oil pool which underlies approximately two sections of our land. There is potential for future development of these lands utilizing a waterflood secondary recovery scheme.

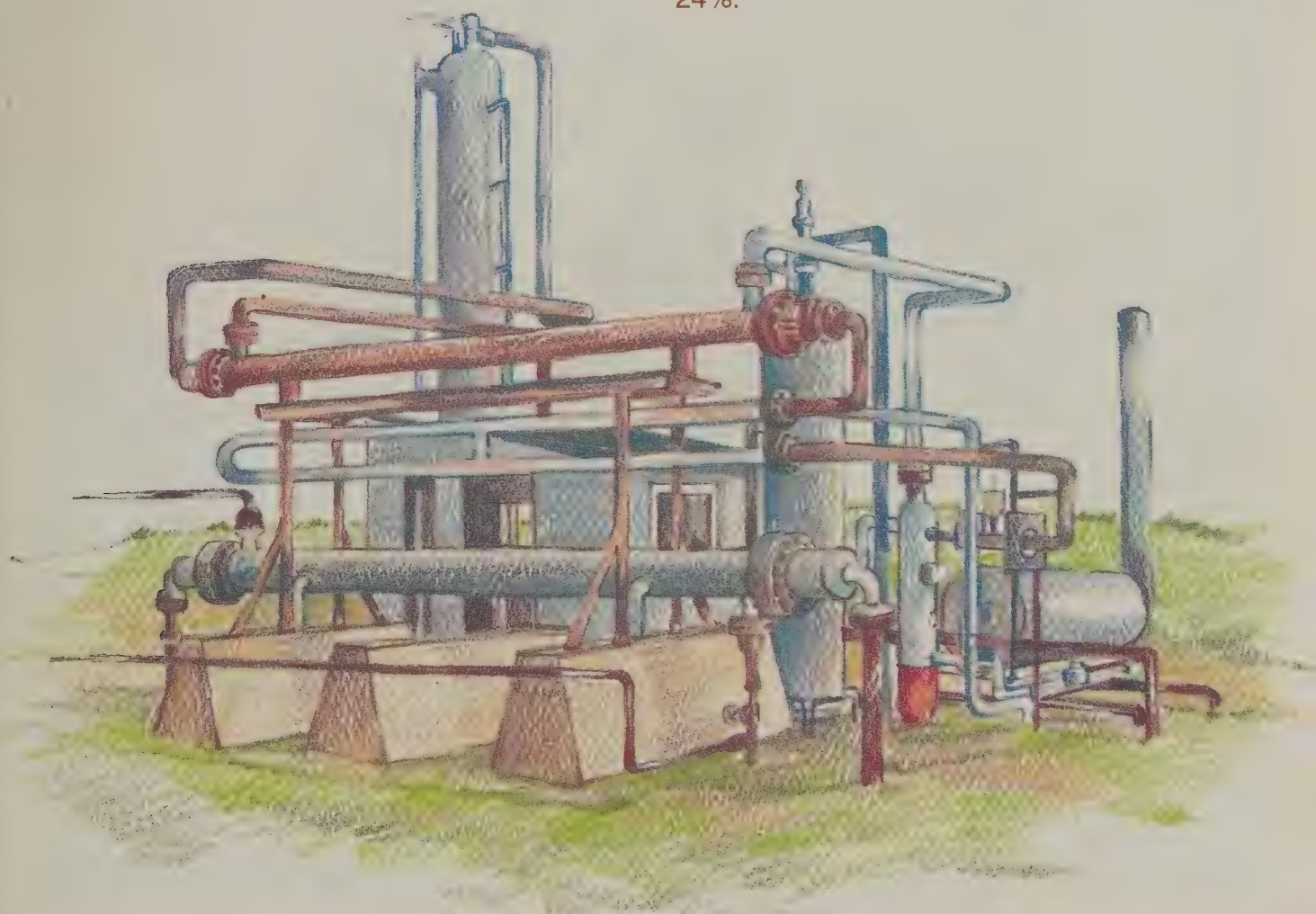
### **Sedalia**

We have an average working interest of 20% in 27,200 acres at Sedalia. We are producing gas from five wells contracted to Northwestern Utilities Ltd. at a rate of 5 MMcf per day with the Company's share averaging 1.25 MMcf

per day. There is production potential in the undrilled acreage and the timing of future drilling will depend upon the gas marketing situation.

### **Stanmore**

Paloma has acquired an interest in 8,800 gross acres (3,226 net acres) through farmout drilling and lease acquisition. In addition, we have a farmout option to earn a further 5,600 gross acres. Drilling, based on seismic surveys, has resulted in two gas wells to date and a number of additional wells are planned for 1977. We have shared in pipeline and plant facilities with other companies operating in the area and we have a contract with Trans Canada Pipe Lines Limited to sell 2 MMcf per day. Our initial share of gas sales will be 24%.





### Acadia

Paloma has interests in 5,760 acres, which were acquired through farmout drilling and lease purchase. We have drilled two successful gas wells which tested gas up to 4.4 MMcf per day. A gas contract is being finalized with delivery to commence in late 1977 and we expect gas sales to be around 1 MMcf per day. The Company's share of sales will be 40.5%.

### Flat Lake

In early 1976 we joined with two other companies in purchasing two sections of prospective gas acreage located within three miles of a pipeline in the Flat Lake area which is 80 miles Northeast of Edmonton. Two successful wells were drilled during the year, each of which tested gas at 1.5 MMcf per day. We do not have a gas contract and have deferred expenditures for a compressor and other facilities. Our interest in the Flat Lake production will be 26%.

### Lait and Kilda

In these two areas, along the South border of the Province of Alberta, the Company owns interest in two shut-in gas wells, both drilled in 1976 and capable of producing around 1 MMcf per day. We have a 42% interest in Lait and a 26% interest in Kilda.

### U.S. Operations

Paloma has land holdings in Arkansas, Oklahoma and Louisiana. In Oklahoma we have an interest in 12,000 acres on the Arkoma Basin on which we plan to develop drilling prospects for farmout to third parties. Along the eastern extension of the Arkoma Basin, in Arkansas, we have a one-third interest in over 100,000 acres. In 1976 we farmed out a 9 section block in exchange for the drilling of a 5,000 foot exploratory well. The well was abandoned after finding gas in non-commercial quantities.

The Company has a 25% interest in approximately 6,500 acres near the Cotton Valley field in Webster County in Northwestern Louisiana. We have negotiated a farmout whereby a third party has paid us a cash bonus and is currently drilling a well in excess of 10,000 feet to earn a 75% interest in these lands. This well will test the Smackover formation which has gas and condensate potential.







# Auditors' Report to the Shareholders

We have examined the consolidated balance sheet of Paloma Petroleum Ltd. as at December 31, 1976 and the consolidated statements of earnings, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1976 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Calgary, Canada  
March 17, 1977

PEAT, MARWICK, MITCHELL & CO.  
Chartered Accountants





## Consolidated Balance Sheet

December 31, 1976

(with comparative figures for 1975)

|                                                                                                                                      | <b>Assets</b>       |                   |
|--------------------------------------------------------------------------------------------------------------------------------------|---------------------|-------------------|
|                                                                                                                                      | <b>1976</b>         | <b>1975</b>       |
| Current assets:                                                                                                                      |                     |                   |
| Cash . . . . .                                                                                                                       | \$ 421,781          | 1,104,110         |
| Accounts receivable . . . . .                                                                                                        | 1,859,521           | 1,280,555         |
| Marketable securities, at cost (market<br>value \$1,049,464) (Note 8) . . . . .                                                      | 484,211             | —                 |
| Inventories, at lower of cost or replacement cost . . . . .                                                                          | 76,724              | 59,467            |
| Prepaid expenses . . . . .                                                                                                           | 16,554              | 21,827            |
| Total current assets . . . . .                                                                                                       | <u>2,858,791</u>    | <u>2,465,959</u>  |
| Property, plant and equipment (Note 2) . . . . .                                                                                     | 18,403,993          | 15,732,365        |
| Less accumulated depletion and depreciation . . . . .                                                                                | <u>2,186,781</u>    | <u>1,507,432</u>  |
|                                                                                                                                      | <u>16,217,212</u>   | <u>14,224,933</u> |
| Other assets:                                                                                                                        |                     |                   |
| Marketable securities, at cost which<br>approximates market value . . . . .                                                          | —                   | 485,631           |
| Agreements for sale receivable, net of<br>current portion . . . . .                                                                  | 127,277             | 172,024           |
| Video tapes, at cost less amortization of \$62,210 . . . . .                                                                         | 373,259             | 435,469           |
| Drilling and other deposits, at cost . . . . .                                                                                       | 70,996              | 60,371            |
| Sundry . . . . .                                                                                                                     | 12,295              | 18,437            |
| Financing costs, at cost less amortization<br>of \$21,602 . . . . .                                                                  | 112,474             | 113,481           |
|                                                                                                                                      | <u>696,301</u>      | <u>1,285,413</u>  |
| Excess of purchase price of subsidiary over fair<br>value of net assets acquired, at cost less<br>amortization of \$27,005 . . . . . | 783,158             | 810,163           |
|                                                                                                                                      | <u>\$20,555,462</u> | <u>18,786,468</u> |

See accompanying notes.



## Liabilities

|                                                      | <u>1976</u>      | <u>1975</u>      |
|------------------------------------------------------|------------------|------------------|
| Current liabilities:                                 |                  |                  |
| Bank loan . . . . .                                  | \$ —             | 122,597          |
| Accounts payable and accrued liabilities . . . . .   | 1,629,533        | 1,338,920        |
| Current portion of long-term debt (Note 3) . . . . . | 2,662,321        | 741,187          |
| Total current liabilities . . . . .                  | <u>4,291,854</u> | <u>2,202,704</u> |
| Long-term debt (Note 3) . . . . .                    | 11,606,851       | 12,580,716       |
| Deferred income taxes . . . . .                      | 1,642,079        | 1,441,933        |
| Minority interest in subsidiary companies . . . . .  | 243,557          | 223,559          |
| Shareholders' equity:                                |                  |                  |
| Share capital (Note 4):                              |                  |                  |
| Common shares without nominal or par value.          |                  |                  |
| Authorized 7,000,000 shares;                         |                  |                  |
| issued 4,139,149 . . . . .                           | 1,171,282        | 1,171,282        |
| Contributed surplus . . . . .                        | 338,000          | 338,000          |
| Retained earnings . . . . .                          | 1,261,839        | 828,274          |
|                                                      | <u>2,771,121</u> | <u>2,337,556</u> |

Approved on behalf of the Board:

 C. J. Williams, Director

 John E. Roberts, Director

\$20,555,462

18,786,468

**PALOMA PETROLEUM LTD.****Consolidated Statement of Earnings****Year ended December 31, 1976**

(with comparative figures for 1975)

|                                                                                                                                            | 1976              | 1975             |
|--------------------------------------------------------------------------------------------------------------------------------------------|-------------------|------------------|
| Revenue:                                                                                                                                   |                   |                  |
| Oil and gas . . . . .                                                                                                                      | \$3,048,384       | 1,965,366        |
| Hotel and real estate . . . . .                                                                                                            | 3,422,570         | —                |
| Other . . . . .                                                                                                                            | 97,019            | —                |
|                                                                                                                                            | <u>6,567,973</u>  | <u>1,965,366</u> |
| Expenses:                                                                                                                                  |                   |                  |
| Oil and gas production . . . . .                                                                                                           | 387,944           | 199,078          |
| Hotel and real estate . . . . .                                                                                                            | 2,719,198         | —                |
| General and administrative . . . . .                                                                                                       | 617,513           | 382,697          |
| Interest on long-term debt . . . . .                                                                                                       | 1,493,701         | 296,433          |
| Depletion . . . . .                                                                                                                        | 389,029           | 104,856          |
| Depreciation . . . . .                                                                                                                     | 351,473           | 49,014           |
| Amortization . . . . .                                                                                                                     | 110,817           | —                |
|                                                                                                                                            | <u>6,069,675</u>  | <u>1,032,078</u> |
| Earnings before income taxes, minority<br>interest and extraordinary item . . . . .                                                        | 498,298           | 933,288          |
| Income taxes:                                                                                                                              |                   |                  |
| Current . . . . .                                                                                                                          | 191,556           | 117,500          |
| Deferred . . . . .                                                                                                                         | 349,646           | 460,600          |
| Province of Alberta Royalty Tax Credit . . . . .                                                                                           | (346,967)         | (304,500)        |
|                                                                                                                                            | <u>194,235</u>    | <u>273,600</u>   |
| Earnings before minority interest and<br>extraordinary item . . . . .                                                                      | 304,063           | 659,688          |
| Minority interest in earnings of subsidiaries . . . . .                                                                                    | 19,998            | —                |
| Earnings before extraordinary item . . . . .                                                                                               | 284,065           | 659,688          |
| Extraordinary item:                                                                                                                        |                   |                  |
| Reduction of deferred income taxes resulting<br>from application of drilling and exploration<br>expenses by certain subsidiaries . . . . . | 149,500           | 75,600           |
| Net earnings . . . . .                                                                                                                     | <u>\$ 433,565</u> | <u>735,288</u>   |
| Earnings per share (Note 5):                                                                                                               |                   |                  |
| Before extraordinary item . . . . .                                                                                                        | \$ 0.07           | 0.16             |
| Extraordinary item . . . . .                                                                                                               | 0.03              | 0.02             |
|                                                                                                                                            | <u>\$ 0.10</u>    | <u>0.18</u>      |

*See accompanying notes.*



# Consolidated Statement of Changes in Financial Position

**Year ended December 31, 1976**

(with comparative figures for 1975)

|                                                                                                            | 1976                        | 1975                  |
|------------------------------------------------------------------------------------------------------------|-----------------------------|-----------------------|
| Source of funds:                                                                                           |                             |                       |
| Net earnings before extraordinary item . . . . .                                                           | \$ 284,065                  | 659,688               |
| Add (deduct) items not affecting working capital:                                                          |                             |                       |
| Depreciation . . . . .                                                                                     | 351,473                     | 49,014                |
| Depletion . . . . .                                                                                        | 389,029                     | 104,856               |
| Amortization . . . . .                                                                                     | 110,817                     | —                     |
| Deferred income taxes . . . . .                                                                            | 349,646                     | 460,600               |
| Minority interest . . . . .                                                                                | 19,998                      | —                     |
| Other . . . . .                                                                                            | (3,871)                     | —                     |
| Working capital provided from operations . . . . .                                                         | 1,501,157                   | 1,274,158             |
| Proceeds on sale of property, plant and equipment . . . . .                                                | 201,492                     | 18,863                |
| Increase in bank loans . . . . .                                                                           | 1,665,000                   | 9,800,000             |
| Marketable securities reclassified as current . . . . .                                                    | 484,211                     | —                     |
| Reduction in agreements for sale receivable . . . . .                                                      | 44,747                      | —                     |
| Issue of 10% note payable . . . . .                                                                        | 15,700                      | 271,580               |
|                                                                                                            | <u>3,912,307</u>            | <u>11,364,601</u>     |
| Use of funds:                                                                                              |                             |                       |
| Purchase of property, plant and equipment . . . . .                                                        | 2,908,465                   | 794,754               |
| Reduction of long-term debt . . . . .                                                                      | 2,654,565                   | 2,575,731             |
| Financing costs . . . . .                                                                                  | 20,595                      | 113,481               |
| Purchase of additional shares in a subsidiary (Note 1) . . . . .                                           | 25,000                      | —                     |
| Net assets acquired on purchase of subsidiaries including working capital deficiency of \$42,416 . . . . . | —                           | 7,855,452             |
|                                                                                                            | <u>5,608,625</u>            | <u>11,339,418</u>     |
| Increase (decrease) in working capital . . . . .                                                           | (1,696,318)                 | 25,183                |
| Working capital at beginning of year . . . . .                                                             | 263,255                     | 238,072               |
| Working capital (deficiency) at end of year . . . . .                                                      | <u><u>\$(1,433,063)</u></u> | <u><u>263,255</u></u> |

See accompanying notes.



# Consolidated Statement of Retained Earnings

**Year ended December 31, 1976**

(with comparative figures for 1975)

|                                        | 1976               | 1975           |
|----------------------------------------|--------------------|----------------|
| Balance at beginning of year . . . . . | \$ 828,274         | 92,986         |
| Net earnings . . . . .                 | 433,565            | 735,288        |
| Balance at end of year . . . . .       | <u>\$1,261,839</u> | <u>828,274</u> |

*See accompanying notes.*

## Notes to Consolidated Financial Statements

**December 31, 1976****1. Accounting policies:**

- (a) The consolidated financial statements include the accounts of all wholly-owned subsidiaries, a 60%-owned subsidiary, Grenville Explorations Limited, and a 91.45%-owned subsidiary, Compass Investments of Alberta Limited. Compass Investments of Alberta Limited has a wholly-owned subsidiary Conquest Oil & Mining Ltd. which has a 80%-owned subsidiary, Compass Resources Ltd. During the year, Conquest Oil & Mining Ltd. acquired an additional 2% of the outstanding shares of Compass Resources Ltd. for a consideration of \$25,000.
- (b) The Company follows the full cost method of accounting for exploration and development expenditures, wherein all costs related to the exploration for and development of petroleum and natural gas reserves are capitalized and depleted on the composite unit-of-production method, based on estimated proven reserves, as determined by independent engineers. Proceeds on minor property sales are credited to the net book value of property and equipment without recognizing any gain or loss on disposition. Gains or losses on major property sales are recognized in the statement of earnings.
- (c) Oil and gas production and processing equipment is depreciated on the composite unit-of-production method. Other equipment is depreciated on the declining balance method at rates varying from 20 - 30 percent, which rates are estimated to amortize the costs over the useful lives of the assets. Depreciation has been provided on assets of the hotel and real estate operations on the straight-line method based on their useful lives as follows:
- |                     |          |
|---------------------|----------|
| Building . . . . .  | 4% - 5%  |
| Equipment . . . . . | 5% - 10% |
- (d) Financing costs are being amortized on the straight-line method over a period of six years.
- (e) The excess of purchase price of subsidiary over the fair value of net assets acquired at date of purchase, is being amortized on the straight-line method over a period of 30 years.
- (f) Video tapes are being amortized over seven years using the straight-line method.
- (g) The Company follows the tax allocation basis of accounting for all timing differences between net earnings and taxable income.



# Notes to Consolidated Financial Statements

## 2. Property, plant and equipment:

|                                                       | 1976                | 1975              |
|-------------------------------------------------------|---------------------|-------------------|
| Oil and gas operations:                               |                     |                   |
| Petroleum and natural gas properties . . . . .        | \$10,131,730        | 8,329,654         |
| Less accumulated depletion . . . . .                  | 1,421,005           | 1,031,976         |
|                                                       | <u>8,710,725</u>    | <u>7,297,678</u>  |
| Production and other equipment . . . . .              | 2,444,261           | 1,583,023         |
| Less accumulated depreciation . . . . .               | 499,264             | 475,456           |
|                                                       | <u>1,944,997</u>    | <u>1,107,567</u>  |
| Total oil and gas . . . . .                           | <u>10,655,722</u>   | <u>8,405,245</u>  |
| Mining properties . . . . .                           | 165,675             | 164,220           |
| Hotel and real estate operations:                     |                     |                   |
| Land, buildings, equipment and improvements . . . . . | 5,662,327           | 5,655,468         |
| Less accumulated depreciation . . . . .               | 266,512             | —                 |
| Total hotel and real estate . . . . .                 | <u>5,395,815</u>    | <u>5,655,468</u>  |
| Total property, plant and equipment . . . . .         | <u>\$16,217,212</u> | <u>14,224,933</u> |

## 3. Long-term debt:

|                                                                                                                             | 1976                | 1975              |
|-----------------------------------------------------------------------------------------------------------------------------|---------------------|-------------------|
| Bank loans . . . . .                                                                                                        | \$11,885,000        | 10,535,000        |
| 7% to 10% first mortgages and agreements<br>for sale, secured by certain lands and buildings,<br>due 1979 to 1988 . . . . . | 1,803,226           | 1,977,906         |
| 10% note payable to shareholder including<br>interest thereon, unsecured, subordinated<br>in favor of bank loans . . . . .  | 287,279             | 271,580           |
| Note payable to affiliated company, unsecured,<br>interest 2% over prime rate . . . . .                                     | —                   | 243,750           |
| Note payable on video tapes, unsecured,<br>non-interest bearing, due 1981 . . . . .                                         | 293,667             | 293,667           |
|                                                                                                                             | <u>14,269,172</u>   | <u>13,321,903</u> |
| Deduct current portion of long-term debt . . . . .                                                                          | <u>2,662,321</u>    | <u>741,187</u>    |
|                                                                                                                             | <u>\$11,606,851</u> | <u>12,580,716</u> |

Although the bank loans are repayable on demand under the terms of repayment, \$9,400,000 of the loans shall be repaid in consecutive quarterly instalments as follows:

|                | Quarterly<br>Repayments | Aggregate of<br>Quarterly<br>Repayments |
|----------------|-------------------------|-----------------------------------------|
| 1977 . . . . . | \$ 300,000              | 1,200,000                               |
| 1978 . . . . . | 500,000                 | 2,000,000                               |
| 1979 . . . . . | 620,000                 | 2,480,000                               |
| 1980 . . . . . | 620,000                 | 2,480,000                               |
| 1981 . . . . . | 620,000                 | 1,240,000                               |
|                |                         | <u>\$ 9,400,000</u>                     |





# Notes to Consolidated Financial Statements

The \$9,400,000 loan is subject to mandatory prepayments to be applied in the inverse order of maturity if operating cash income (as defined) exceeds on a quarterly basis, the payments referred to above, such mandatory prepayments are estimated to be \$450,000 in 1977.

Approximately \$745,000 of the balance of the bank loans of \$2,485,000 will be repaid in 1977.

The bank loans are secured by an assignment of the Company's interests in certain petroleum and natural gas properties, assignments of book debts and a pledge of the shares of Compass Investments of Alberta Limited. In addition, a subsidiary has issued, as additional security, a first floating charge debenture in the principal amount of \$3,000,000 and an assignment of sale proceeds of certain land and buildings of \$2,300,000. Interest is at the rate of 1½% over the prime lending rate.

Under the terms of the bank loans, certain requirements are placed on the Company with regard to maintenance of consolidated working capital and shareholders' equity. In addition, the payment of dividends is restricted.

#### **4. Share capital:**

At December 31, 1976 the company has reserved 150,000 common shares for issue in exchange for the shares owned by all the minority shareholders of a subsidiary company. The shares will be issued for an aggregate value of \$337,500. This transaction is subject to the approval of certain regulatory authorities.

#### **5. Earnings per share:**

Basic earnings per share is calculated using the weighted average number of shares outstanding during the year.

Fully diluted earnings per share, after giving effect to the issue of common shares as referred to in note 4, are not presented as there would be no material change.

#### **6. Remuneration:**

The aggregate remuneration paid to directors and senior officers during the year amounted to \$179,033 (1975 — \$220,840).

#### **7. Anti-Inflation Act:**

The Company is subject to the provisions of the Anti-Inflation Act and Regulations governing the amount of dividend payments and as a result the amount of dividends which may be paid is restricted.

#### **8. Subsequent event:**

On January 4, 1977 the Company sold its marketable securities for an aggregate consideration of \$1,049,064 which resulted in a gain of approximately \$401,000, net of income taxes.





**PALOMA PETROLEUM LTD.**

**DIRECTORS:** Walter J. Adams, Edmonton, Alberta  
G. Clarence Elliott, Winnipeg, Manitoba  
W. Roy Jennings, Calgary, Alberta  
D. M. Laurence, Calgary, Alberta  
William H. Molle, Toronto, Ontario  
John E. Stobart, Calgary, Alberta

**OFFICERS:** Walter J. Adams, Chairman of the Board  
D. M. Laurence,  
Deputy Chairman of the Board  
John E. Stobart, President  
Norman F. Talbot, Secretary-Treasurer

**HEAD OFFICE:** 1150 Guinness House  
727 - 7 Avenue S.W.  
Calgary, Alberta  
T2P 0Z7

**TRANSFER AGENT  
AND REGISTRAR:** Montreal Trust Company  
Calgary, Vancouver, Toronto, Montreal

**LEGAL COUNSEL:** McLaws & Company  
Calgary, Alberta

**AUDITORS:** Peat, Marwick, Mitchell & Co.  
Calgary, Alberta

**BANKERS:** The Toronto-Dominion Bank  
Main Branch, Calgary

**SUBSIDIARY COMPANIES:** Compass Investments of Alberta Limited  
Compass Resources Ltd.  
Conquest Oil & Mining Ltd.  
Conquest Resources, Inc.  
Grenville Exploration Limited  
Grizzly Petroleum Limited  
Paloma Petroleums, Inc.





**PALOMA PETROLEUM LTD.**

ANNUAL REPORT 1976